



March 12, 2004

Ms. Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, DC 20551

Re: Docket No. R-1176 Comments to Regulation CC Amendments

Dear Ms. Johnson:

The Association of Corporate Credit Unions (“ACCU”) would like to express our appreciation for the opportunity to comment on a proposed rule to amend Regulation CC and its commentary to implement the Check Clearing for the 21st Century Act (the “Check 21 Act”) and improve Regulation CC overall. ACCU further applauds the Federal Reserve Board for thoroughly inspecting the proposal and for the extended comment period it offered on the rule. ACCU is the primary trade association for the country’s corporate credit unions (“corporates”) located around the country. Corporates provide liquidity, investment products, payments settlement and other financial services to the nation’s federal and state-chartered credit unions.

ACCU supports the letter of comment submitted to the Board of Governors of the Federal Reserve System by the Credit Union National Association regarding the proposed changes discussed herein and in their letter of comment. ACCU also worked in conjunction on this letter with two of its members, Empire Corporate Federal Credit Union and Mid-Atlantic Corporate Federal Credit Union, and fully support their respective comment letters as well.

Legal Equivalence for Substitute Checks with MICR Errors

ACCU believes all substitute checks should be treated as the legal equivalent of the original check regardless of whether there is an error in the MICR line of the substitute check. This will ensure that a substitute check is a reliable, negotiable instrument.

Currently, the proposal would make certain MICR line errors a reason to deny the legal equivalence of a substitute check. By allowing this, the proposal introduces new liabilities and timing impediments into the check collection system and will create uncertainty regarding the handling of substitute checks. We believe that all substitute checks should be considered the legal equivalent of its original regardless of errors on the

MICR line. Moreover, financial institutions should be given the same rights in handling substitute checks with MICR line errors as they are currently given with regard to the original.

The final rule should require a reconverting bank to print the MICR information from the original check on every substitute check that it creates. A failure by the reconverting bank to do so should be considered a breach of the Check 21 Act Warranties.

Encourage MICR Repair on Substitute Checks

ACCU strongly believes that the reconverting bank, collecting bank and returning bank should be allowed to repair MICR line errors on a substitute check without invoking the Check 21 warranties and thus incurring additional liability for consequential damages under the Check 21 Act. We also believe that the proposal should encourage collecting and paying financial institutions to treat and repair the MICR lines on substitute checks in the same manner that they would treat and repair original checks. As with original checks, these repairs should not be mandatory. If the collecting or paying financial institution repairs the MICR line of a substitute check incorrectly, they should incur the liabilities for breach of the encoding warranties under the Uniform Commercial Code (“UCC”) and Regulation CC.

By making a downstream financial institution liable under the warranties of the Check 21 Act, these institutions will be discouraged from making such corrections as they are doing today. We believe this will lead to an increase in errors at the consumer level that do not exist under current regulation.

Ultimately, if the reconverting bank does not place a MICR line on a substitute check that matches the original check’s MICR line, and another credit union or consumer experiences a loss, then the warranties and indemnities under the Check 21 Act as written should and would protect that person. The warranties and indemnities under the Check 21 Act from the reconverting bank will protect subsequent parties to the extent any liability arises from the receipt of a substitute check with MICR line information that does not “accurately represent” the MICR line information on the original check.

Address Inconsistent Liability Among Reconverting Banks

ACCU strongly supports amending the proposed regulation to create equivalent liability among the first and second reconverting bank, when the first reconverting bank does not provide notice that it is creating a substitute check. If the first reconverting bank does not properly encode position 44 of the MICR line, the second reconverting bank may not recognize the item to be a substitute check and thus the second bank may create an illegal substitute check by failing to preserve the size of the image of the original check. We believe that under the proposed regulation, the second reconverting bank would be liable for consequential damages as a result of an error by the first reconverting bank. The first reconverting bank would further be absolved of their breach of the warranties under Check 21. We request the Federal Reserve Board to amend the commentary of the proposed regulation to state that the second reconverting bank will not bear liable for consequential damages due to an error by the first reconverting bank.

Eliminate Concept of “Purported Substitute Check”

ACCU requests the elimination of Section 229.51(c)) of the proposed regulation, which discusses the concept of a “purported substitute check”. We believe this section introduces uncertainty into the reliability of substitute checks.

Definitions and Standards

ACCU supports including the new definition of “transfer and consideration” in the proposal. This will allow a paying financial institution to transfer a substitute check to its members or customers.

ACCU believes that the Federal Reserve Board should refer to general industry standards in the regulation and reserving any discussion of specifics within these standards for the Commentary. This will allow the Federal Reserve Board to support an industry standard without having to amend its regulation beyond the Commentary when this standard is adjusted or changed at some point in the future.

Adopt “Banking Day”

ACCU supports incorporating the usage of “banking day” in the proposal, as opposed to “business day”. By doing so, the regulation would be consistent with the timing in Regulation E.

The Proposal Should Apply to the Check 21 Act Substitute Checks and the Check 21 Act Warranties

ACCU supports excluding duplicate ACH debit payments that originate from a substitute check from the Check 21 Act warranties. The NACHA Operating Rules provide proper protection for consumers under this scenario.

Consumer Disclosures

ACCU supports the following items as they regard consumer disclosures:

- Shortening the consumer awareness notice to include only the basic information on substitute checks and expedited recredits, so that it is easier for a consumer to read.
- Including sample notices for the Check 21 Act notice requirements and specifying that the Federal Reserve Board deems usage of these, or substantially similar notices, as compliance with the Act.
- Eliminating the requirement to notify consumers in writing when a claim is valid. In these cases, the consumer will receive a recredit.
- Allowing financial institutions, which have not already provided disclosures, to provide a consumer awareness notice with the substitute check.

Unrelated Regulation CC Amendments

ACCU requests that the Federal Reserve Board take the following comments into consideration as they regard unrelated Regulation CC amendments.

- ACCU supports adopting a new Regulation CC warranty regarding unsigned, remotely created items, after the Federal Reserve Board develops a specific warranty that undergoes the rulemaking process.

These new warranties should be similar to the warranties recently adopted by the National Conference of Commissioner on Uniform State Law for UCC Articles 3 and 4.

- ACCU does not support reduction of the time frames for notice of nonpayment. For checks in the amount of \$2,500 the time frames should remain as they are.
- ACCU generally supports requiring disclosures in Regulation CC to be consistent with the requirements of the Electronic Signatures in Global and National Commerce Act (the E-Sign Act) and adopting language that clarifies the acceptability of e-mail.
- ACCU supports the concept of defining “clear and conspicuous,” for purposes of notices under Regulation CC, after the Federal Reserve Board develops a specific proposal that undergoes review in a normal comment process. This proposal is not part of the Check 21 Act, and therefore is not subject to the time restrictions of Check 21. As a result, the Federal Reserve Board should present the public with the specific language, so that organizations can provide meaningful comments, before this language is implemented.
- ACCU supports the Federal Reserve Board’s proposal to allow more flexible usage of notices. The Board proposes adding a sentence to the commentary to § 229.10 (c) to clarify that a special deposit slip notice need not be posted at each teller window, although it must be posted in a place where consumers are likely to see it before making a deposit.
- ACCU supports the Federal Reserve Board’s proposal to define “local bank” more clearly.
- ACCU supports clarification of the current rules regarding the extension of the Midnight Deadline. The proposed amendment to Regulation CC would make it clear that the check must be received by the returning bank’s cutoff hour for the next check-processing cycle.

Additional Comment

In addition to the comments provided in CUNA’s letter, ACCU would like to support an issue concerning reconverting banks raised in Empire Corporate Federal Credit Union’s comment letter dated March 9, 2004. This issue of concern presents itself when a person other than a bank creates a substitute check for the purpose of depositing such checks for collection. The first bank that receives a substitute check from a non-bank that transfers (or presents or returns) the substitute check is defined as a reconverting bank. Definition of “Reconverting Bank,” Section 229.2 (yy). Although on page 71 of the supplementary information to the proposed rule, it does state that a non-bank may only transfer a substitute check it created only by agreement. This might be an area that might need some clarification

If you have any questions regarding ACCU’s comments, please do not hesitate to contact me.

Very truly yours,

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Mike Canning

Executive Director, ACCU